

Testimony before the

Committee for Purchase from People Who Are Blind
or Severely Disabled

Regarding Proposed Regulations
of Governance and Executive Compensation
for Non-profit Agencies

January 26, 2006
San Francisco, CA

Good morning, I am Bill Mead, the CEO of Job Options, a CRP located in San Diego.

- I. Overview of the issues
 - a. Concerns are valid
 - i. I share the Committee's concerns regarding compensation and governance. The JWOD program has suffered as a result of one sided media attention, but the issues are complex and will not yield to simple solutions.
 - b. The issues are complex
 - i. Executive compensation
 - 1. The issue of executive compensation not simple. Ideally, salaries should reflect a number of aspects of job performance including: an organization's success; its complexity; staff satisfaction; and the education requirements of the position. Salaries must also reflect the market, because non-profits must complete with all other businesses.
 - ii. Board governance
 - 1. The issue of board governance is similarly complex. CRPs vary widely in size with annual revenues from under \$100,000 to more than \$100,000,000. This great variation in size means that CRPs and their boards vary widely in sophistication and resources.
 - iii. Consequences

1. The complexity of these issues suggests simple formulaic solutions will result in serious injustices and unintended consequences.

II. Governance

- a. Governance must be evaluated by outcome not process. A board of three members who never change but who provide quality oversight for a non-profit that consistently attains goals, treats its employees with respect and is financially sound is unquestionable superior to a board made up of 12 or more members who rotate regularly but who delegate total authority to the staff. Simple inflexible rules regarding size and turnover only address the surface.
- b. One of the unintended consequences of mandating large board size is the increased control that is delegated to the executive staff. Large boards, like large groups generally as has been documented by studies of the bystander effect, dilute individual responsibility. In a very large board the power devolves to executives, thus negating the intended outcome. Similarly, board turnover insures that board members are always on a steep learning curve. This, also, puts more power in the hands of the executive staff. *Power will follow knowledge*, and a board that isn't knowledgeable will always be subordinate to executive staff.

III. Executive compensation

- a. Too much attention has been give to large salaries. This is natural because they make headlines, but the public's perceptions of salaries can be unrealistic. The \$90,000 the Committee has identified as the threshold of high compensation strikes me as quite low. I personally know secondary school teachers who earn 6 figure salaries. A salary in Southern California of \$90,000 is the going rate for a controller not a CEO.
- b. People with disabilities deserve competent leadership. This is leadership committed to providing good employment in a supportive environment. Executives with these skills are in demand and receive good salaries. Limiting salaries of CEOs simply penalizes an already disadvantaged population.
- c. I must admit that the issue of the impact of compensation on fair market prices confuses me. If these are fair market prices then aren't they fair and a reflection of the market? The procurement officers with whom we work drive hard but fair bargains. If there are procurement officers that would support a high salary for me, I'd like their phone numbers.

IV. Recommendations

- a. General

- i. In general I'd like to recommend to the Committee that it adopt a supportive partnership approach to these problems. Solutions should start with analyses of causes. For example, do boards know what is required of them? Do boards have the expertise and resources to exercise their responsibilities?

b. Governance

- i. Using this approach, I would like to suggest that the Committee, working with an organization like BoardSource, develop a portfolio of training materials and standards. It should set requirements for rebuttable presumption of reasonableness for salaries. As a last resort the Committee should consider sanctions for CRP boards that fail to meet minimum standards.
- ii. The Committee should mandate board training that could be provided by the CNAs or an organization like BoardSource. This training should be provided in geographically diverse areas and should be subsidized for small CRP boards.
- iii. I would strongly urge the Committee to avoid setting rigid requirements for board size, composition and turn over. Board performance should be measured by outcomes related to CRP performance and board oversight.

c. Compensation

- i. Again, I would urge the Committee to avoid setting strict limits for compensation, and I am very concerned that the Committee considers \$90,000 to be high compensation. Rather, the Committee should, through board training, insure that boards are acting responsibly and legally in discharging their responsibilities. The Committee should accept evidence of rebuttable presumption of reasonableness for executive compensation.
- ii. It has been suggested that CEO salaries should be linked to the salary of the lowest paid staff member. This approach, while emotionally appealing, would have dire unintended consequences. CRPs should be hiring people of low productivity because it is these individuals who are least likely to be otherwise employed. The most successful CRP by this measure would then have to pay its CEO the lowest salary. I doubt that's the Committee's intention.
- iii. Finally, I believe the Committee should work closely with the Internal Revenue Service to insure that CRPs suspected of paying the CEOs unreasonably high salaries are properly investigated. The IRS has the expertise and resources to do this kind of investigation and evaluation.

V. Summary

- a. Adopt a supportive partnership approach.
- b. Avoid “one size fits all solutions” to complex problems.
- c. Insure good board governance through mandatory and subsidized board training.
- d. Accept rebuttable presumption of reasonableness as sufficient justification for compensation and refer problem CRPs to the IRS.
- e. Consider the impact on Committee resources if complex issues are going to be subject to intense scrutiny.

VI. Thank you for allowing me to share my thoughts with you.

Stephanie Hillmon

From: William Mead [meadwilliam@hotmail.com]
Sent: Sunday, January 29, 2006 7:37 PM
To: Stephanie Hillmon
Subject: Committee hearings in San Francisco
Attachments: Responses to specific Committee issues.doc; C4P testimony final text.doc

First, I want to correct my testimony before the Committee last Thursday. I was caught off guard when asked about my annual compensation, and, as you may remember, I had to do a little quick mental arithmetic. Upon my return I checked my numbers with my controller and she pointed out that an incentive payment I actually received in 2006 was reported as 2005 compensation. The amount of this payment was \$60,000 and my total annual compensation was \$226,000 not the \$168,000 I recall having quickly calculated. My controller also indicated that I may receive an additional amount once all the incentives are fully evaluated, but this amount should not exceed an additional \$20,000. I appreciate the opportunity to set the record straight.

I have attached two documents. One is the full text of my intended testimony before I pared it down to 5 minutes. The second document contains responses to the specific points the Committee made in its announcement.

Again, I appreciate having had the opportunity to testify. I was impressed with the articulateness of my colleagues and the thoughtfulness of the Committee's questions and remarks. I think it's clear we all want to have a positive impact on unemployment among people with disabilities.

Responses to specific Committee issues:

Governance

1. Yes, board members should be committed, but I don't know how you would measure that. Generally, just being will to serve is evidence of commitment.
2. Not only should an employee board member not be able to influence the board unduly, I don't think employees should be board members at all. Having the CEO be an *ex officio* and non-voting member has some appeal, but my experience is that CEOs have plenty of input and influence on their boards and board membership is neither necessary nor advisable. Boards need as much independence as they can get.
3. Setting the lower limit at 5 is reasonable, and the board chair and CEO should not be the same. As I stated above, I don't believe the CEO should be a board member.
4. Term limits is a difficult issue since it is hard for even larger CRPs to attract competent board members. I would suggest more flexible language, which at least insures rotation of board officers. Boards should be able to provide evidence of recruitment to support their efforts to find new members and to avoid the consequences of imposed term limits.
5. The board should reflect the diversity of the community with regard to disability, gender, race, ethnicity and geography. In some communities sexual orientation is an important issue and needs to be reflected in board membership.
6. Board members should serve without compensation except for expenses. This should be a rigid requirement.
7. Yes, a board should have a committee structure that includes executive search, executive evaluation and compensation. The board should evaluate highly compensated individuals annually or periodically if executives serve under an employment contract.
8. Board evaluation of overall compensation is a good idea.
9. Boards should review and approve audits and approve plans to implement recommendations.

10. Boards should have written conflict of interest policies that identify areas of concern and disclosure procedures.
11. While having a financial expert, as defined by the Committee, is a good goal, it is not necessarily practical. One would have to be a CPS to qualify and CPAs are in demand on boards and hard to recruit. Boards need to be able to rely on their auditor for expertise, and they should fully explain findings to them. The definition of “financial expert” needs to be broadened to include any individual who has financial expertise beyond the usual person. This could include a controller or head bookkeeper, an individual in the banking industry or the treasurer or CFO of a business. These individuals are knowledgeable, but do not necessarily have audit experience.
12. Agencies should periodically review compliance and the boards should be intimately involved in any such review.
13. The publication of the data indicated is helpful in creating an atmosphere of openness and should be followed.
14. The process of rebuttable presumption of reasonableness should be followed carefully for all highly compensated staff.

Additional governance issues.

1. Yes, these criteria are sufficiently comprehensive.
2. Broadening the definition of financial expert, prohibiting employees from serving on boards and loosening the turnover requirements would be reasonable.
3. I am not impressed with accreditation. I personally know of a non-profit that is CARF certified where the board delegates far too much responsibility to the executive staff. (N.B. the organization is not mine.) It is much too easy to “con” auditors from accrediting bodies. Accreditation related to social service organizations, such as CARF, is an expensive and largely useless exercise. Job Options is ISO 9001 certified and that is a far more effective and valuable accreditation that is meaningful to our government and non-government customers. It doesn’t address issues of governance in a way that is responsive to the Committee’s concerns, however. The Committee should develop its own methods of insuring good governance and should annually randomly sample CRPs for governance audits.

4. All CRPs should be subject to the same criteria regardless of affiliation or size. If good governance is important, and it is, it's important for all organizations.
5. Vide supra
6. This is the most difficult task. Again, boards should be judged by outcomes, not process. Do their agencies meet mission goals? Are their employees satisfied? Is there organization financial sound? Do they fully document communication and rebuttable presumption of reasonableness? Do they have the necessary board procedures to insure adherence to the law? These are the things the Committee should audit.
7. For participating non-profits, the Committee should establish criteria to be reported on annually. Periodic site visits should also be done to check documentation. Concerns about salaries should be referred to the Internal Revenue Service, with whom the Committee should establish a close working relationship. For central non-profits, the Committee needs to do much more in-depth evaluation of actual functioning. Staff, board members and CRP opinions should be sampled regarding their perceptions of the effectiveness of the CNAs. The Committee should consider re-bidding these contracts periodically through a challenge process whereby potential challengers would have to demonstrate a *prima facie* case that it would be better able to meet the needs of the JWOD system. If a challenger demonstrated that, the Committee should issue an RFP and formally re-bid the CNA.
8. There are filing requirements that document some aspects conflict of interest. Documentation should be available to demonstrate that the non-profit doesn't do business with any board member. Where this is unavoidable, such as in small towns, the arms length nature of all transactions needs to be documented and made available to the Committee.
9. The Committee should review agencies' basic financial ratios annually. They should receive copies of audit reports and review Dun and Bradstreet reports. Agencies should be able to document access to resources, either through agency assets or lines of credit, necessary to meet at least 90 days operating needs.

Fair Market Prices

1. I don't believe there is a clear relationship between executive compensation and proposed fair market prices. The Committee should continue to rely on the expertise of procurement officers to negotiate a fair price. I believe there is the presumption that high executive salaries are a problem, but a close look

at the data suggests that there are small agencies with a much higher proportion of their revenues being dedicated to salaries than is the case with large organization with more highly paid executives.

2. No, there shouldn't be a *de minimis* test. As I said above, there are low paid executives of small agencies that receive a questionable amount of their agency's revenues. Rather, the Committee should rely on procurement officers to do their jobs faithfully.
3. No. There can be no absolute value that could be considered as affecting fair market prices. Large executive salaries are typically paid in very large organizations and in those cases executive salaries represent a much smaller proportion of agency revenues than in small agencies with lower paid executives.
4. Yes, rebuttable presumption of reasonableness should be accepted as demonstration that the fair market price is not unduly affected.
5. There should be no relationship. In an agency that serves individuals with very significant impairments, wage will be low, but executive salaries shouldn't be proportionally lower. Salaries should reflect ability and results.
6. I don't believe there is a relationship between pricing and executive compensation. Compensation should only be reviewed if rebuttable presumption of reasonableness doesn't support the level of compensation being paid, and this should be referred to the IRS for resolution.
7. Since agencies should be following a rebuttable presumption of reasonableness approach, they should file these data with the Committee. The Committee could then monitor that process.

Other issues.

Sub-minimum wages

1. The issue of sub-minimum wage was given considerable attention during the oral testimony. In keeping with many of my colleagues, I like the idea of paying no less than the Federal minimum wage to employees and in fact Job Options doesn't pay less than minimum wage. We are primarily a service provider, and that makes it easier for us because our jobs don't lend themselves well to workers with very severe impairments. Product producers and disability specific agencies like ARCs, however, do have very low productivity workers and paying no less than the Federal minimum wage would be a serious hardship for them. The result again would be an

unintended consequence. Either these agencies would drop out of the JWOD program or they would have to eliminate the sub-minimum wage employees.

In another agency with which I have been associated we had clients who were unable to work many hours and as a consequence earned very small wages. As was pointed out, though, there is more than the total dollar amount involved in what these people earn. First, there is the idea that they are actually earning anything. Receiving a paycheck, no matter how small, makes them feel like they are more a part of society as a whole, which defines self worth to a large extent in term of work. Secondly, many very low paid workers are in what are essentially work/activity programs. These are therapeutic activities and the paycheck is part of that therapy. Finally, an overlooked fact is that these individuals usually subsist on SSI benefits, and after paying for a board and care homes they are lucky to have \$20 a month for incidentals. If these individuals earn only \$5 a week they have doubled their discretionary income, and while it's not a lot of money it has an impact on them that is probably similar to that which the rest of us would experience if our discretionary income doubled. It provides the means for simple pleasures that the rest of us take for granted. These include such things as a movie, a meal at a fast food restaurant or a new tee shirt.

As much as it would be ideal for everyone to earn at least the Federal minimum wage, for some the consequences would be dire. If this is going to be the Committee's decision, it must identify a way to pay for it.

Collective bargaining

Collective bargaining was also the subject of oral testimony. Some members of the Committee voiced the opinion that CRPs should not be allowed to resist unionization. Before continuing let me say that Job Options has unions in a couple of its locations and this has not been a problem for us. These unions are sensitive to the unique aspects of JWOD, and thus we have an excellent working relationship. There are some unions that we would probably resist and in the past we resisted the Teamster's Union.

It should be noted that our experience is that the desire to unionize is not a desire that arises from our employees. Rather, when it occurs it comes about because of union proselytizing. In such a situation, denying us the right to tell our side of the story would be a denial of free speech rights, and as such is probably not constitutional. The Labor Relations Act provides employees plenty of protection and insures that the process is fair. Interference in this well regulated process would not be a useful.

CRP employees should have the same rights regarding unionization as any other employee and they do. They should be given both sides arguments and be allowed to decide.

Thank you again for allowing me the opportunity for these comments.

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Job Options, Inc.

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